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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1944

Nos. 379 and 380

COLORADO INTERSTATE GAS COMPANY, a Corporation, PETITIONER,

v.

FEDERAL POWER COMMISSION, CITY AND COUNTY OF DENVER, COLORADO, PUBLIC SERVICE COMMISSION OF WYOMING, COLORADO-WYOMING GAS COMPANY, PUBLIC SERVICE COMPANY OF COLORADO, and CANADIAN RIVER GAS COMPANY, RESPONDENTS.

CANADIAN RIVER GAS COMPANY, a Corporation, PETITIONER,

v.

FEDERAL POWER COMMISSION, CITY AND COUNTY OF DENVER, COLORADO, PUBLIC SERVICE COMMISSION OF WYOMING, COLORADO-WYOMING GAS COMPANY, PUBLIC SERVICE COMPANY OF COLORADO, and COLORADO INTERSTATE GAS COMPANY, RESPONDENTS.

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

REPLY BRIEF OF COLORADO INTERSTATE GAS COMPANY AND CANADIAN RIVER GAS COMPANY, PETITIONERS, IN SUPPORT OF PETITIONS FOR WRITS OF CERTIORARI

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The belated brief filed by the Respondents in opposition to the petitions of Colorado Interstate Gas Company and Canadian River Gas Company for writs of certiorari in their respective cases is apparently tendered and filed as a common brief for both cases, although as far as Petitioners have been informed, no order of consolidation has been entered. Following, however, the procedure of the Respondents, Petitioners will join and make this one reply to the common brief of the Respondents captioned in the two cases.

In this reply we shall use the same abbreviations used in the petitions for the writs and the briefs filed in support thereof.

Colorado Interstate's petition for writ sets forth and presents four separate and independent questions. Canadian's petition for writ sets forth and presents nine separate and independent questions.

Respondents in their brief state to this Court that there are only four questions presented in these two applications for writs, which they set forth in their brief. We respectfully submit that there are thirteen separate and independent questions presented by the two petitions, and these are the thirteen questions set forth in the two petitions, and Respondents cannot dispose of the questions presented by the petitions by ignoring them or indicating, as they have, that such questions are not before this Court.

This reply brief is rendered necessary only because the Respondents have thought it proper either to entirely ignore or avoid the questions presented by Petitioners, or, where they have purported to answer any of our questions, they have, in many instances, based their answer upon inaccurate or misleading references to the record.

We will not in this reply re-argue our questions presented, but will limit the reply to calling the Court's attention to the points which have been ignored and avoided by counsel for the Respondents and to the portion of counsel's argument which is based upon the inaccurate and misleading references to the record.

Exercise of Prohibited Rate Regulatory Jurisdiction Over Production and Gathering

This is Question No. 1 presented by Canadian in its petition (page 3), with the reasons in support thereof set forth at pages 27, et seq. It is entirely ignored and avoided by the Respondents; it is not listed in Respondent's brief as being among the "questions presented." The Congress of the United States, in Section 1(b) of the Act, has expressly provided that the Commission should not have jurisdiction over production or gathering. In the Hope case this Court said, not once, but twice, that the Commission has no jurisdiction over production and gathering. (Pages 287,

289, Vol. 88, L. Ed., Advance Opinion.) The Circuit Court in its opinion in this case expressly holds that the Commission does not have rate regulatory jurisdiction over production and gathering. (R., V. 8, 5075) The law of this case is, therefore, that the Commission does not have jurisdiction over production and gathering. The Respondents have not applied for any writ directed to the holding of the Circuit Court that the Commission does not have such jurisdiction, and, of course, are bound by the law of the case as established by the Circuit Court. The question presented by Canadian's Question No. 1 is not whether the Commission has jurisdiction over production and gathering because the law of the case is that it has not, but the question is whether what the Commission did, and which the Circuit Court approved, does not constitute an exercise of jurisdiction over production and gathering, which the Act, the Circuit Court, and this Court have held is prohibited. This question is absolutely ignored and avoided in Respondents' brief. For reasons pointed out in Canadian's petition, the question is of such great importance as to justify the granting of the writ directed thereto. We do find a short footnote at pages 18 and 19 of Respondents' brief, possibly intended to be a passing casual recognition that this point is included in the case, although obviously the footnote has no bearing upon the text to which it is a footnote. In this footnote the Respondents contend that if the Commission does not have jurisdiction over production and gathering, it could not fix reasonable rates for interstate transportation and sales, as required by the Act. Support is sought to be found for this statement in the opinion of this Court in the Hope case. Clearly no such support can be found in that case. Where this Court discussed production and gathering in the Hope case, it stated, not once but twice, that the Commission did not have jurisdiction over production and gathering. No question of such jurisdiction was raised by the Hope Company, such as raised in this case, and the discussion there had was with reference only to the position taken by the State of West Virginia and clearly has no bearing at all upon the question here presented.

Moreover, as we have pointed out in the reasons in support of this point, it is not impossible for the Commission to exercise its delegated jurisdiction over interstate trans-

portation and sales without exercising a prohibited jurisdiction over production and gathering. The evidence established a commodity value of Canadian's gas at the wellhead in the field and at its gathering system termini. The Commission could have used this commodity value of Canadian's gas as the starting point for the exercise of its delegated jurisdiction over interstate transportation and sale and avoided any usurpation of prohibited jurisdiction over production and gathering.

The Commission held that it does have jurisdiction over production and gathering. The Circuit Court ruled that it does not, but further held that what the Commission did does not constitute an exercise of jurisdiction over production and gathering. The Respondents make no attempt here to support the Circuit Court in the Court's ruling that what the Commission has done does not constitute regulation of production and gathering. The Respondents still insist, however, (without having applied for any writ to reverse the Circuit Court), that the Commission does have jurisdiction over production and gathering.

We submit the determination of the question presented, so completely ignored and avoided by Respondents, should be assumed by this Court.

Valuation of Canadian's Leasehold Properties

In Question No. 2 presented by Canadian it is pointed out that, even assuming arguendo that the Commission has rate regulatory jurisdiction over production and gathering, it is improper in determining a production and gathering rate base, to limit the value of gas leaseholds to their original cost of acquisition, generally speaking on a "wildcat" value basis while in the hands of predecessor companies to the exclusion of all discovery, market or other values. The result of such procedure adopted by the Commission is to limit Canadian's return, as far as its gas leaseholds are concerned, generally to 6½% per annum, on a nominal value and, in many instances, on a zero value, as some of Canadian's now most valuable leases were acquired without cash consideration, and in consideration of drilling obligation only. Canadian contends (even assuming rate regulatory jurisdiction) that original cost is not the proper basis

for the inclusion of gas producing leaseholds in a rate base, and that the Commission has erred in blindly following its original cost and prudent investment theories with respect to Canadian's gas leaseholds and in wholly disregarding uncontroverted evidence of value.

Respondents, in their brief, have absolutely ignored and entirely avoided this question. They do not even make a casual reference to its existence as one of the questions presented. We submit that Respondents' silence recognizes the merit to this question.

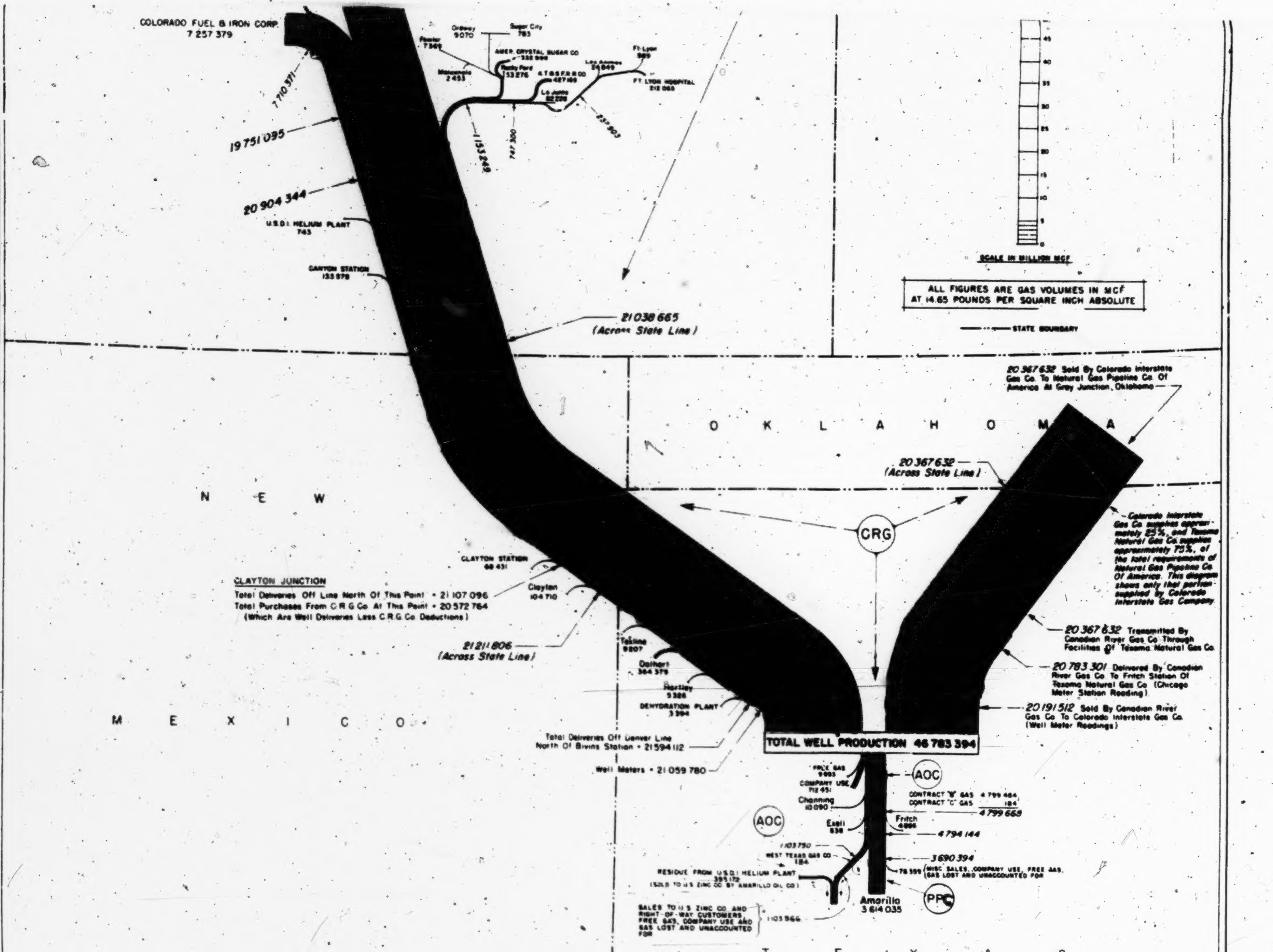
Abrogation of the Cost Reimbursement Provisions of the Cost Contract

The error in the Commission's action in abrogating the cost reimbursement provisions of Canadian's cost contract is presented in Question No. 4 in Canadian's petition, with reasons in support thereof set forth on pages 19 and 20. This again is ignored in Respondents' statement of questions proposed to be presented, although on page 20 of their brief they ask this Court to affirm the death penalty against Canadian in reliance upon Chicago B. & Q. R. R. Co. v. Iowa, 94 U. S. 155, 162-163. This case, we submit, is entirely inapplicable, and, if it could be construed as supporting Respondents' contention and thus requiring Canadian to do the impossible (as Respondents' brief impliedly admits), it is certainly contrary to and inconsistent with the "rate impact" and "end result" principles announced by this Court in the Hope case.

Original Cost of Properties

This question is discussed in Canadian's petition (pages 8-10, 17-19, 31-33) and in Colorado Interstate's petition. (Pages 6-9, 17-21.)

Respondents, in their answer brief, (pages 10-14) attempt to answer Canadian's contentions on the theory that the transaction whereby Canadian acquired certain properties from Amarillo Oil Company was between affiliates and, as a matter of fact, constituted no sale at all. This argument is fallacious. The record clearly shows there was a sale which resulted from prolonged, arm's-length bargaining between



COLORADO FUEL & IRON CORP.
7 257 379
7 710 371
19 751 095
20 904 344
U.S.D.I. HELIUM PLANT
743
CANYON STATION
133 578
Ordway
9070
Sugar City
783
Fowler
7 369
Manzanola
2 453
AMER. CRYSTAL SUGAR CO
Rocky Ford
53 276
A.T.& S.F.R.R.CO
427 169
La Junta
Las Animas
Ft. Lyon
FT. LYON HOSPITAL
1 153 249
747 300
21 038 665
(Across State Line)
SCALE IN MILLION MCF
ALL FIGURES ARE GAS VOLUMES IN MCF AT 14.65 POUNDS PER SQUARE INCH ABSOLUTE
STATE BOUNDARY
O K L A H O M A
20 367 632 Sold By Colorado Interstate Gas Co. To Natural Gas Pipeline Co. Of America At Gray Junction, Oklahoma
20 367 632
(Across State Line)
CRG
N E W
M E X I C O
Colorado Interstate Gas Co. supplies approximately 25%, and Texoma Natural Gas Co. supplies approximately 75%, of the total requirements of Natural Gas Pipeline Co. Of America. This diagram shows only that portion supplied by Colorado Interstate Gas Company
CLAYTON STATION
68 431
Clayton
104 710
CLAYTON JUNCTION
Total Deliveries Off Line North Of This Point = 21 107 096
Total Purchases From C.R.G.Co. At This Point = 20 572 764
(Which Are Well Deliveries Less C.R.G.Co. Deductions)
21 211 806
(Across State Line)
Texline
9207
Dalhart
364 379
Hartley
5 386
DEHYDRATION PLANT
3 394
20 367 632 Transmitted By Canadian River Gas Co. Through Facilities Of Texoma Natural Gas Co.
20 783 301 Delivered By Canadian River Gas Co. To Fritch Station Of Texoma Natural Gas Co. (Chicago Meter Station Reading)
20 191 512 Sold By Canadian River Gas Co. To Colorado Interstate Gas Co. (Well Meter Readings)
Total Deliveries Off Denver Line North Of Bivins Station = 21 594 112
Well Meters = 21 059 780
TOTAL WELL PRODUCTION 46 783 394
FREE GAS
COMPANY USE
712 451
Channing
10 090
AOC
CONTRACT "B" GAS 4 799 484
CONTRACT "C" GAS 184
4 799 668
Fritch
Exell
638
4 794 144
1 103 750
WEST TEXAS GAS CO
184
3 690 394
RESIDUE FROM U.S.D.I. HELIUM PLANT
395 172
(SOLD TO U.S. ZINC CO. BY AMARILLO OIL CO.)
76 359 MISC. SALES, COMPANY USE, FREE GAS, GAS LOST AND UNACCOUNTED FOR
SALES TO U.S. ZINC CO. AND RIGHT-OF-WAY CUSTOMERS, FREE GAS, COMPANY USE AND GAS LOST AND UNACCOUNTED FOR
1 103 566
Amarillo
3 614 035
PPC

non-affiliated companies and that Five Million Dollars in cash was paid for such properties.

The purchase of the wells, gas rights, and leaseholds from Amarillo Oil Company was a condition precedent to the launching of the enterprise. It did not constitute, in any sense, a pooling of assets as suggested by Respondents. The money, when paid, belonged to Amarillo Oil Company to use as it desired without let or hindrance so far as the other parties were concerned. The project might have failed completely, but even so, Amarillo Oil Company would have retained as its own, the full Five Million Dollars received for the property it sold. This being true, neither the case of Niagara Falls Power Co. v. Federal Power Commission, 137 F.2d, 787, nor the other cases cited by the Respondents have any bearing whatsoever upon the question submitted.

Respondents also intimate (pages 12-13) that Amarillo Oil Company received only $310,000.00 of the purchase price. This statement is erroneous. Commission staff witness Luttring testified unequivocally as follows:

> "Ultimately the Amarillo Oil Company received by way of credits, or otherwise, the full amount of the purchase price of Five Million Dollars." (R., V. 5, p. 2938).

He also stated that the bulk of the Five Million Dollars was distributed by Amarillo Oil Company to Southwestern as a dividend. (R., V. 5, 2938)

The fact that Canadian carried the alleged profit made by Amarillo Oil Company on its books as "Appreciation" and that no income taxes were paid at that time has no significance whatsoever. Certainly this method of handling the matter does not change the actual *fact* as reflected by the uncontradicted evidence in this Record. Southwestern filed a consolidated income tax return for the period covered by the sale, which return reflected all of the operations of all of its subsidiaries, including Amarillo Oil Company and Canadian. (R., V. 5, 2638, 2639, 2905, 2906). This necessarily resulted in the elimination of any profit as well as any loss from an income tax standpoint, but it also resulted in a lower depreciation base for Canadian, and, in the long run, will probably result in the payment of more income taxes rather than less.

The "Appreciation" so called was carried on the books of Canadian purely for income tax purposes and merely as a matter of bookkeeping convenience. Its only purpose was to show the correct depreciation base that resulted from the consolidated income tax return. It was not a writeup, as intimated by Respondents, in any sense of the word. It resulted in no entry whatsoever in the surplus account. (R., V. 5, 2637) Had it been a writeup, it necessarily would have been reflected in that account.

The primary reason and perhaps the only reason that Commission staff and Commission ignored this arm's length sale was the fact that an alleged profit was made by Amarillo Oil Company and the further fact that the Commission considered the transaction as a purchase and sale between affiliated companies. (R., V. 8, 2908)

If we should assume, for the purpose of the argument, that the transaction did constitute a sale between affiliated companies, even this would not justify the action taken by the Commission and its staff. This very principle has been decided by the Supreme Court in the case of American Telephone and Telegraph Company vs. United States, 299 U. S. 232, 240; 81 L. Ed. 142. Mr. Justice Cardozo, speaking for a unanimous court, held definitely and positively that even where properties were purchased from an affiliated company, that if the difference between the purchase price and the cost to the selling company represented *a true increment of value*, such profit could not be written off or ignored. This rule has been followed and applied in the recent case of New York Telephone Company v. United States of America, et al., decided by a three judge court, Southern District of New York on August 24, 1944. (This case not yet reported.)

There is not the slightest intimation in the Record in this case that the properties purchased by Canadian were not worth every dime paid for them. In fact, the Record clearly shows that the property was worth far more than the purchase price paid.

We shall not here re-argue Colorado Interstate's contention that the Commission and the Court erred in eliminating from original cost or prudent investment the cost of certain

contracts. The respondents merely answer this contention by asserting that they were transactions between affiliates, which is entirely incorrect, and Colorado Interstate's petition and brief show conclusively that this was an arm's length transaction between companies, neither of which had any interest in the other.

Life of Canadian's Reserves

This question was discussed in Canadian's petition, pages 6, 7, 20-22, 36-38.

The respondents, in their answer, pages 14-16, contend that there was an issue of fact as to the life of Canadian's reserves, and further, that it doesn't make any difference anyway whether such reserves last fifty-three years or twenty-seven years or any other period.

Respondents cite testimony of Commission Witness Hammer to the effect that such reserves had a life of 73.7 years. This reference is misleading. Respondents did not refer to all of the testimony of such witness. The witness made it very clear on cross examination that this figure (73.7 years) "was used only in an illustrative manner and it was not his conclusion as to the life of Canadian's reserves." He testified further that he had arrived at no definite conclusion with respect to the life of such reserves, and had merely attempted to arrive "at a reserve beneath the Canadian River acreage * * * as of August 1, 1939." And whether Canadian would recover the entire amount of reserves as estimated "is a question that isn't * * * directly associated with an estimate of reserves." (R., V. 7, 3999) This testimony completely and directly refutes Respondents' contention.

It is true that the Commission stated in its opinion that theoretically, migration of gas is automatically accounted for under the "pressure decline method" and is actually accounted for if the isobaric maps are properly drawn. It is perfectly apparent from the Commission's opinion that it was referring, in this connection, to the *estimate of reserves* made by Commission staff. (R., V. 1, 158-159) This finding, therefore, has no relevancy whatsoever with respect to the *life* of Canadian's reserves. The Record clearly shows, without contradiction, that the life of a portion of an intercon-

nected reservoir where drainage exists, cannot be determined by estimating the reserves under the portion in question, and then dividing this by the estimated future annual production from that portion only. Even if there were any evidence in the Record that the *life* of such reserves could be determined in such manner, and there is not, such evidence would be so completely contrary to fundamental natural laws that no court or commission could logically accept such testimony.

What the Commission witness did say was that *he had made no study of drainage at all*, and that his isobaric map took into consideration only *certain drainage factors* and that "it does not adjust itself completely to the drainage question." (R., V. 6, 3641) *The witness was also speaking of his reserve estimate only, and not with respect to the life of Canadian's reserves.*

We state unequivocally that there is not a single line of testimony in this record that would support a finding that the life of Canadian's reserves can be determined in the manner in which the Commission attempted to determine such life. On the other hand the Record positively, affirmatively, and without contradiction, establishes the fact that such life cannot be determined by the method followed by the Commission. If we resolve all disputed questions of fact with respect to the life of Canadian's reserves in favor of the Commission's determination, such life does not exceed twenty-seven years from December 31, 1939.[1]

The Respondents, however, take the position that the Circuit Court has found that the Record does not disclose that the Commission failed appropriately to weigh the "existing volume, pressure differentials and consequent drainage and other recovery factors." We again direct the attention of the court to the fact that the Circuit Court there was speaking

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[1] This Court, in the case of Thompson, et al. v. Consolidated Gas Utilities Corporation, et al., 300 U.S. 55, 71; 81 L. Ed. 510, 519, recognizes the drainage situation existing in the Texas Panhandle Field and that gas in such field migrates or drains throughout the field from areas of high pressure to areas of low pressure. There is nothing in this Record that would, in any manner, cause this Court to make a different finding as to drainage at this time.

only of reserve estimates and was not referring in any sense of the word to the life of such reserves. (R., V. 8, 5091)

Moreover, the very fact that the Commission determined Canadian's recoverable reserves to be 2,800,000,000 Mcf, and then determined the life thereof simply by dividing into this figure, an estimated future annual production of fifty-five million Mcf., shows conclusively upon its face that the Commission did not take drainage into account, but necessarily assumed that Canadian would produce every cubic foot of recoverable reserves under its acreage. (R., V. 1, 159)

The Respondents then say, (Pages 15-16) referring to the Commission's opinion that it makes little difference whether the life of Canadian's reserves was properly determined or not if consistency is maintained in computing the annual expenses and the accrued depreciation and depletion. We submit that it does make a difference even though the Commission's theory of "consistency" is followed and that this difference amounts, so far as both Canadian and Colorado Interstate are concerned, to a very substantial sum per year for each company in net earnings.

Canadian's Revenues Available for Return

This question was discussed in Canadian's petition, Pages 22-24, 38.

The Respondents, in their answer, Footnote, Page 21, state, contrary to Canadian's contention, that Commission's Accountant did actually restate Canadian's revenues as well as its expenses on an accrual basis for the test year. This statement is very misleading. The Accountant did restate Canadian's income on an accrual basis *in some particulars*. He did not adjust Canadian's income with respect to that portion of rate case expense and income taxes actually paid in cash in 1939, but allocated to other years on an accrual basis.

The adjustments made in income are clearly reflected in Exhibit 168. (R., V. 6, 3419, 3421) It will be noted that three items only were included in this adjustment, two of them being debits and one a credit; but none of such adjustments included the items here in question. This resulted

in a net deduction of income in the sum of $54,708.28. The total income as shown by Canadian's books was $2,448,095.27. (R., V. 6, 3415) This income, as adjusted by the Commission Accountant, was $2,393,386.99, (R., V. 6; 3417), or a total deduction of exactly $54,708.28. It will be noted also that the Commission, in its opinion, found Canadian's income as adjusted to be $2,393,387.00 (R., V. 1, 171) being the exact amount determined by the Commission's Accountant. It is perfectly apparent, therefore, that neither the Commission nor its Accountant made any adjustments whatsoever in the income account by reason of the elimination of the items complained of in the expenses for the year 1939. The court will bear in mind that under the "Cost Contract," income always balanced precisely with cash expenditures and, therefore, both income accounts and expense accounts were necessarily kept on a cash basis. Assuming the Commission was correct in eliminating some of the cash expense items, then it became absolutely necessary to make the same adjustments in income for the reason that the income was determined absolutely by the expenses and had such expenses not been incurred in that year, the income would have been less by that precise amount.

Respondents also contend that rates were not affected by reason of the Commission's treatment of the $15,056.24 adjustment made by reason of the alleged profits of Amarillo Oil Company in the extraction of gasoline. This is also a misleading statement. The record shows clearly that the Commission Accountant credited the production expense of Canadian with the amount of the alleged profit made by Amarillo Oil Company and thus reduced Canadian's production expenses in 1939 by this exact amount. This necessarily resulted in increasing Canadian's revenues available for return in this same amount. (R., V. 6, 3425, 3461, 3462, 3466, 3472) Respondents strangely refer to the allocation study made by a Commission witness. (R., V. 4, 2317, 2382) This witness merely deducted the amount of Amarillo Oil Company's alleged profit from the cost of gas it had purchased from Canadian, and thus showed a smaller figure for gas purchased. This allocation study, by the wildest stretch of the imagination, can have absolutely no relevancy to the question here presented. It dealt with an entirely different

subject and its only purpose was to develop a formula with respect to the allocation of cost as between regulated and nonregulated business. The fact that the Commission did actually reduce Canadian's operating expenses by the amount of this alleged profit, did result in the regulation by it of Amarillo Oil Company's purely intrastate transactions over which the Commission had no jurisdiction and which had absolutely no relationship to Canadian's operations.

Respondents also contend that the question with respect to Texas gross production taxes paid by Canadian was raised for the first time in the Circuit Court. This question was raised in the Motion for Rehearing filed with the Commission.[2] (R., V. 1, 265) Respondents' statement that an excessive allowance for income taxes would more than offset this has no relevancy whatsoever. It is absurd to say that Canadian would have no taxable income if, as a matter of fact, it will have a net income in excess of $600,000. (R., V. 1, 173)

Depreciation as an Annual Operating Expense

This question was discussed in Canadian's petition, pages 24, 25, 38-40.

Respondents on page 16 of their answer brief, make the contention that Canadian is seeking to place in the rate base, and amortize, future replacements, and they say that this was condemned by this Court in the Natural Gas Pipe Line Case. We make no such contention.

We simply contend that the Commission's testimony reflects clearly and without question that it will be necessary for Canadian to make replacements of property now in use at a cost of $6,500,000 during the service life of the enterprise as determined by the Commission.

Colorado Interstate's contention with respect to the allowance for annual depreciation and amortization not being sufficient to take care of interim replacements that will have

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[2]The footnote on page 24 of Canadian's petition states that the Act of the Texas Legislature which increased gross production taxes became effective May 1, 1944. This was a typographical error. The Act became effective May 1, 1941.

to be made, fully presented in its petition and brief, has been ignored and avoided by Respondents, and accordingly we do not undertake to re-argue this matter here.

An unbroken line of authorities which have been approved in principle by this Court hold that in a limited life project such as this one, the company must accrue over the life of the project (1) a fund sufficient to enable it to replace physical properties that will be worn out prior to the termination of the project, and in addition thereto (2) a fund sufficient to return to it the value of its properties upon the termination of the project.

The depreciation and depletion allowances made by the Commission are wholly inadequate to accomplish this. Such allowances should be increased sufficiently to enable Canadian and Colorado Interstate to make these necessary replacements.[3]

Allocation

The Respondents make no answer to our contentions in this respect. They impliedly concede, and the Record clearly shows, that they considered both Canadian and Colorado Interstate as one composite system in the development of the allocation formula. This being true, there was no basis to make any reduction whatsoever in the price of that portion of the gas sold by Canadian to Colorado Interstate for direct pipe line industrial sale.

We might also add that Section 1 (b) of the Natural Gas Act must necessarily be read in connection with Section

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[3]The opinion in the Natural Gas Pipe Line Case (315 U.S. 575) does not condemn Canadian's contentions with respect to this issue. The Court stated on page 592 that an item for future capital additions through 1954, *including replacements* amounting to $12,159,380 was included in the amortization base. Footnote 9 on the same page discloses that of this amount, $9,146,683 constituted the cost of additional properties or future capital additions. It is apparent, therefore, that the cost of replacements totaled approximately three million dollars. The cost of these replacements was actually included in the amortization base and this action was not condemned by the Court. We are not here asking that replacements be placed in the rate base or, in any sense, amortized. We merely say that the Commission committed error in failing to allow sufficient annual depreciation and amortization allowances, considering only the property presently in service, to enable Canadian and Colorado Interstate to make such necessary replacements. As a matter of fact, the opinion in the Natural Gas Pipe Line Case may be cited to support our contention.

1 (a) of the Act which empowers the Commission to regulate gas sales that are made for ultimate distribution to the public and not otherwise. Clearly the sales of gas to direct pipe line and industrial consumers is not governed by the terms of the Act.

In Colorado Interstate's petition and brief decisions of this Court are cited to the proposition that in a case of this kind there must be an allocation of property, which the Commission admittedly did not make. These cases are disposed of by the assertion that they do not prevent the use of such a formula as the Commission adopted. We shall not attempt here to re-argue that question.

Also, in Colorado Interstate's petition and brief numerous glaring imperfections were pointed out in the application of the formula which the Commission did use. All of this, however, is utterly ignored and avoided by Respondents, and we shall not re-argue that matter here.

Financial History

On page 20 of the reply brief it is stated:

> "Nor does the financial history of the enterprise sustain the validity of a 'confiscation' argument on the part of Colorado and Canadian."

They then cite certain figures showing, with respect to Colorado Interstate, the dividends paid, the reserves accumulated for depreciation and amortization of contracts, surplus, and reduction of debt, up to December 31, 1939, and as to Canadian they show how much of its total cash investment had been recovered in cost of gas up to December 31, 1941. Respondents fail to advise the Court, however, that Canadian has never paid a dividend. The Commission has found that Canadian is entitled to a net return of $609,375 annually, which is at the rate of 6½% on the rate base found by the Commission. This sum of $609,375, multiplied by the 13½ years between the time of Canadian's organization and December 31, 1941, would total $8,226,562 of net return to which the Commission concedes Canadian was entitled, but which was not paid out by way of dividends, but

is reflected in the debt reduction commented upon by Respondents in their answer brief.

The obvious purpose of such a recitation was, of course, to persuade the Court to deny the petitions for certiorari, regardless of the many reasons assigned therefor, most of which are wholly unanswered and many of which are not so much as mentioned.

Among the reasons why the figures set forth have no bearing on the question of the legality of the Commission's order, and accordingly have no proper place in the brief, we will discuss only three:

1. These earnings of Colorado Interstate, and the alleged earnings of Canadian, are from their entire operations. No attempt has been made by counsel, nor has any attempt been made by any of the witnesses, to show what part of these earnings resulted from sales for resale, and what part thereof resulted from direct industrial sales over which the Commission has no jurisdiction whatsoever. As to Colorado Interstate, we invite the Commission's attention to the very large volume of direct industrial sales, as shown on the Commission's own flow map attached to Colorado Interstate's petition as an appendix. The evidence showed that Canadian also had received substantial revenue from direct sale industrial gas, and, in addition, that Canadian received substantial revenue from its intrastate sales in Texas, over which, of course, the Commission had no jurisdiction.

We submit that it is worthless to bring in figures of this kind from the total operations without attempting to advise the Court, as they could not, what portion of the total revenue was derived from sales for resale in interstate commerce, which is the limit of the Commission's jurisdiction.

2. The earnings so shown for Colorado Interstate and the alleged earnings of Canadian covered the period from the beginning of their operations in June, 1928, to December 31, 1939 for Colorado Interstate and to December 31, 1941 for Canadian. For ten years of these respective 11½-year and 13½-year periods neither Colorado Interstate nor Canadian was subject to regulation. Is the Commission to

be permitted, when in 1939 it launches upon a consideration of reasonable rates pursuant to the Natural Gas Act passed in June, 1938, to go back and take into consideration the earnings of the companies for the ten-year period when the companies were subject to no regulation whatsoever? We submit that the question answers itself. We submit also that consideration of such earnings for the ten-year period cannot properly be invoked as a cloak to cover other imperfections in the Commission's Findings and Order.

3. Even if the companies had been under regulation throughout the period of their operations, still their past earnings could no more be used to justify confiscatory rates for the future than past losses, (if they had had them), could be used to justify increased rates for the future; and so this Court has expressly held. In *Board of Public Utility Commrs. v. New York Teleph. Co.*, 271 U. S. 23, the Court in a unanimous opinion (Mr. Justice Stone not participating) on page 32 said:

> "* * * Past losses cannot be used to enhance the value of the property or to support a claim that rates for the future are confiscatory. (Citing cases from this and other courts.) And the law does not require the company to give up for the benefit of future subscribers any part of its accumulations from past operations. Profits of the past cannot be used to sustain confiscatory rates for the future. (Citing cases from this and other courts.)"

This doctrine, even then so well established, was reaffirmed in *Los Angeles G. & E. Corp. v. Railroad Comm.*, 289 U. S. 287. On page 313 the Court said:

> "* * * Deficits in the past do not afford a legal basis for invalidating rates otherwise compensatory any more than past profits can be used to sustain confiscatory rates for the future. Public Utility Comrs. v. New York Teleph. Co., 271 U. S. 23."

The "End Result" and "Rate Impact" Principles Announced in the Natural Gas Pipeline and Hope Cases

In Question No. 9 presented in Canadian's petition we have analyzed the "end result" or "rate impact" effect of the Commission's order on Canadian. Respondents, in their brief, in so far as they have attempted to make any answer to the questions presented, have directed their argument (with inaccurate and misleading references to the Record, as hereinabove pointed out) to certain specific matters selected by them, but they have again totally ignored and avoided the question presented as to whether the Commission's order can be sustained under the "end result" and "rate impact" principles announced by this Court in the Natural Gas Pipeline and Hope cases. On pages 40-42 in Canadian's petition we have sumarized our position as to why the order cannot be sustained under these principles so announced by this Court. We submit that the author of Respondents' brief was fully convinced as to the merit of our position, and, being unable to suggest an answer which could be justified, decided to ignore and avoid the point entirely. Canadian earnestly contends that the basic reasoning behind the "end result" and "rate impact" principles announced by this Court in the Natural Gas Pipeline and Hope cases requires the Commission's order as to Canadian to be set aside and the Circuit court's affirmance thereof reversed.

Other Points Presented

As we have pointed out, Canadian's petition contains nine questions presented and Colorado Interstate's petition contains four questions presented. Respondents' brief avoids some of the most important questions entirely, and bases its answer to other questions upon inaccurate and misleading references to the Record. It is not our intention here fully to present all of the reasons advanced by Colorado Interstate and Canadian in support of all of the questions presented, as this would be an unnecessary repetition of the reasons and arguments set forth in the petitions and briefs filed in support thereof. As to any question presented in either of the petitions which is not specifically referred to in this reply, it should, of course, be understood that we are not waiving any such questions, but we consider that our position is fully set

forth in the reasons and arguments advanced in connection with the petitions and that nothing is set forth in Respondents' brief with reference thereto requiring further argument or reply.

Respectfully Submitted,

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